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RUEHBU/AMEMBASSY BUENOS AIRES 0113
RUEHBY/AMEMBASSY CANBERRA 1377
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TREASURY FOR NEPHEW; IMB (MURDEN, MONROE, CARNES)

E.O. 12958: N/A
TAGS: CA ECON EFIN
SUBJECT: CANADA: INFORMATION FOR SUMMIT ON FINANCIAL
MARKETS AND THE WORLD ECONOMY

REF: A. STATE 114420
¶B. OTTAWA 1372
¶C. OTTAWA 1362

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¶1. (sbu) Ref a requests information regarding Canada's perspectives and concerns regarding the November 15 Summit on Financial Markets and the World Economy -- and also regarding the financial crisis' impact on Canada and government actions to address the crisis. Also per ref a, Econcouns John Carwile (tel: 613-688-5227; email: carwilejl@state.gov) is post's primary point of contact on financial crisis/summit matters.

¶2. (sbu) The following points are keyed to ref a's inquiries:

¶I. Key Objectives and Priorities

Canada is looking to support G-7 -- and in particular, U.S. -- leadership in crafting an approach that uses market-based solutions and that respects a liberalized trading system. Canadian officials and other G8 diplomats here tell us that Canada is still formulating its specific approach to the Summit. Canada has said publicly and privately that the draft Communique is very much headed in the right direction. We understand that Canada will be looking for the following general outcomes:

-- Canada wants to work closely with the United States and other like-minded countries to fight off ideological attacks against capitalism and open markets at the Summit. Canada believes that the financial crisis arose from regulatory failure, and not from a failure of open markets;

-- Canada believes that new regulatory structure is needed, and that many countries will call on the United States to increase its own financial regulation;

-- Canada is keen to have a defined, action-oriented work plan to guide near-term work after the Summit. It is important, Canada believes, that the all Summit participants support the work plan; and

-- Canada supports including the G-20 at the Summit, but says there "are a number of very angry members of the G-20 who feel that the G-7 should have protected them from this crisis." Canada hints that they will want to play an intermediary role between countries calling for a dramatically new global financial architecture and those having qualms about giving the G-20 a bigger seat at the table. (Comment: We suggest that such a role for Canada might be discussed by our Sherpa/sous-sherpas with their Canadian counterparts. End comment)

II. Key Concerns

Canada wants to ensure that G-7 stewardship remains central to the international financial system -- and that a considered follow-on process identifies the causes of and the principles/actions for addressing the crisis. Canada wants to ensure that the international financial remains
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market-based. From Canada's domestic economic perspective, the two most important issues are overall liquidity and

financial guarantees. Canadian officials are confident in their banks' health, but are hoping to minimize the spillover effect from the U.S. markets.

III. Impact of the Financial Market Crisis on the Financial Sector

The World Economic Forum ranks Canadian banks as the world's healthiest; no Canadian bank is near collapse. Canada's regulatory oversight has strict reserve and capital requirements -- and banks are well-capitalized. Canadian investment banks are part of retail banking -- and brokerages meet regulatory requirements pertaining to retail banking. Canadian banks carry a small percentage of sub-prime mortgages (five to six percent of the Canadian mortgage makert is sub-prime; banks hold some 75 percent of Canadian mortgages). Nevertheless, the Toronto stock exchange has fallen dramatically this year. Canada has also suffered from tightening credit flows with the large spreads between Bank of Canada lending rates and commercial bank lending rates. Retail banks, for example, only passed along to consumers half of the 50 basis cut in the Bank of Canada prime rate to consumers on October 8. (Comment: One senior private bank official told us October 29 that the domestic banking sector has enough liquidity, and is being hurt by lower than normal demand for loans -- primarily from the manufacturing sector. End comment)

IV. Actions Taken to Address the Financial Crisis

The Bank of Canada acted with the Federal Reserve, Bank of England, European Central Bank, Sveriges Riksbank (Sweden), and Swiss National Bank to cut their overnight target rate by 50 basis points on October 8. The Bank of Canada further lowered its rate to 2.25 percent on October 21.
www.bank-banque-canada.ca/en/press/2008/pr08- 21.html and
www.bank-banque-canada.ca/en/fixed-dates/2008 /rate 211008.html

The Bank of Canada will provide up to C$ 20 billion in liquidity to banks and has broadened the range of collateral that the Bank will accept.
http://www.fin.gc.ca/news08/08-074e.html

The Bank of Canada and the Federal Reserve have a reciprocal currency arrangement -- currency swap facility -- of US$ 30 billion (if needed) to maintain USD liquidity in the Canadian financial institutions. To date, the Bank of Canada has not needed to use the arrangement.
www.bank-banque-canada.ca/en/notices fmd/2008/not071008.html

Finance Canada will buy up to C$ 25 billion in insured mortgages through the Canadian Mortgage and Housing Corporation to provide Canadian banks with cash with an aim to maintain the availability of longer-term credit for consumers, homebuyers, and businesses.
http://www.fin.gc.ca/news08/08-075e.html

Finance Canada established the Canadian Lenders Assurance
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Facility to federally insure private interbank lending -- as long as the debt has at least a three-month term. The Facility will expire on May 1, 2009. Participating financial institutions will pay a base fee of 1.35 percent, plus a surcharge ranging from 25 to 50 basis points, depending on their credit ratings. (Canada's action parallels steps taken by other countries to guarantee loans, and is designed to

keep Canadian banks competitive in the international lending market.) http://www.fin.gc.ca/news08/08-080e.html

Canada has decided -- so far -- not to increase the C$ 100,000 federal insurance on deposits in Canadian banks.

¶V. Current economic situation/near-term outlook.

See Ottawa 1372. The U.S. Department of Treasury also has provided post with this information: "The Bank of Canada "estimates growth to decelerate to 0.6 percent in 2008, and to be 0.6 percent in 2009. Canadian credit conditions have deteriorated significantly while equity prices have plunged by over 25 percent. Core inflation remained within the central bank's target range of one percent to three percent; inflation risks are likely diminishing from a weakening economy and declining global commodities prices. The health of the auto sector is at the top of Canadian officials' minds."

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